PISM POLSKI INSTYTUT SPRAW MIĘDZYNARODOWYCH
THE POLISH INSTITUTE OF INTERNATIONAL AFFAIRS

NO. 154 (1584), 21 JULY 2020 © PISM

BULLETIN

The Pandemic-Related Economic Crisis in Spain

Maciej Pawłowski

The forecasts by the European Commission (EC) and the International Monetary Fund (IMF) indicate a deepening of the economic crisis in Spain. The Pedro Sánchez government's actions stopped an increase in unemployment and protect the poor, but the liquidity of companies remains under threat. In response, the government has introduced aid programmes for strategic industries and seeks political consensus on a recovery plan for the country. The rising costs of fighting the crisis are to be financed by increased taxes and EU aid.

The Scale of the Crisis. According to the IMF's June forecast and the EC's July forecast, the Spanish GDP will decrease by 10.9-12.8%. That 2-4.8 percentage points (pp) more than these institutions estimated in April and May, respectively. In the whole last century, the Spanish economy was in a worse condition only in 1936 (when GDP dropped by 24.2%), as the civil war broke out. According to the EC forecast, Spain is among the EU Member States most affected by the crisis (GDP decline of 9-11.2%), joining Italy, Croatia, France, Portugal, Slovakia, and Greece.

The tourism, automotive, and aviation industries, which altogether generate about 31% of GDP, are in the most difficult situation. Each sector has recorded a significant decrease in turnover compared to the corresponding periods of 2019. The number of tourists arriving to Spain as of the end of April was down by 50% over the previous year and air travel had dropped by 94%. These losses will not be made up by domestic tourism. According to the Social Research Centre, 65.7% of Spaniards don't plan to go on holiday. At the same time, according to the Spanish Car and Truck Producer's Association, by the end of the year car sales will decrease by 45%.

Government Actions. Because of the decline in the number of infected, on 21 June the government abolished the state of emergency that had lasted from 13 March and introduced a period it called the "New Normality". Social-economic liberties were re-established but the sanitary recommendations remain. Services, sports facilities, museums, and libraries must provide conditions for social distancing and disinfection. The new period will be removed once the pandemic has fully passed.

The government's actions have aimed to soften the social costs of the crisis. After the loss of 900,000 jobs in the period 12-27 March, a temporary law (ERTE, lasting until 30 September) allowing companies to suspend employees was established. That stopped an increase in unemployment (14.5% in May compared with 14.8% in April). The state pays the suspended employees up to 70% of their average salary, but not less than €501.98 and not more than €1,411.83. Suspending utilities to apartments is also prohibited until 30 September. The government has established an allowance of €461-1,110 for about 1.1 million households in which no one has any income.

A credit line worth €140 billion was established to help companies and the self-employed maintain liquidity and employment. Entities that use it must have a registered office in Spain and documented losses as a result of the pandemic. Moreover, entities listed in the Central Risk Register of the Bank of Spain, that divert profits to tax havens, or were in bankruptcy before the pandemic are excluded access to the credit. The loan cannot be used to unify or restructure a company or to repay debts incurred before 18 March 2020. The maximum repayment term is five years.

Government aid programmes for important industries were established. A fund of €10 billion is designated to saving strategic companies in security, healthcare, infrastructure, transport, and the general functioning of the market. The state can buy their stocks and bonds or grant loans to them

in return for the right to a share of their profits. The €250 million "Renovation 2020" programme was established to help the automotive sector. It assumes co-financing in the amount of €300-4,000 (depending on the model) for car purchases made between 16 June and 31 December 2020. The programme is intended to help the industry increase its revenues by €1.1 billion and create 7,400 jobs. A €4.26 billion tourism recovery programme may help to reduce losses in that sector through, for example, the suspension of companies' loan payments and distribution of grants for projects increasing innovation, ecology, and digitalisation of services. Of the total, €23 million has been allocated to rural tourism development.

The Economic Recovery Plan. The government established a parliamentary commission to build consensus for an economic recovery plan. The commission listed 50 "conclusions" on healthcare, social policy, economics, and European policy. On 3 July, these conclusions were approved in the first vote, thanks to the support of MP's from the governing Spanish Socialist Workers Party and Unidas Podemos, and from opposition liberal party Ciudadanos. A boycott by the conservative party Vox helped as well. Some regional parties, including separatists, voted against it because they are worried about the potential centralisation of power through the national plans on social policy and healthcare. The centre-right People's Party rejected conclusions on economics and social policy perceiving them as too protectionist, but its members abstained on healthcare and EU issues and declared their will to negotiate with the cabinet before the second vote.

The plan assumes an increase in state spending. The healthcare budget will increase to 10% of GDP until 2023 and aims to improve medical staff working conditions and the elimination of patient co-payments for medical services. Stable funds to fight unemployment, extend the moratorium on interruptions of utilities, and state support for paying off housing debt remain to be ensured. An increase in the education budget, co-financing of apartment renovations, and the creation of supply-chain protection plans in the automotive and tourism sectors are demanded as well. The plan also establishes a flexible mechanism for using the ERTE as needed during the crisis.

The government's tax plans include raising the upper thresholds of personal (PIT) and corporate (CIT) income taxes from 2021, and is considering an increase in VAT. Funding from the EU is needed as well. Because of Spain's high public debt (95.5% of GDP in 2019), the key issue is to receive grants rather than loans. An acceleration of the introduction of the SURE mechanism, giving access to loans subsiding employment, is important to avoid a drastic increase in unemployment. Spain also demands the establishment of a digital tax at the EU level and argues that the Common Agriculture Policy should be a tool for the ecological transformation of the farming industry. The creation of a sanitary union by transferring to the EC competences enabling it to respond to future pandemics, test Member States' healthcare systems, list approved drugs, vaccines and medical equipment, and coordinate research into the development of a COVID-19 vaccine, are proposed as well. The main Spanish allies in European policy are Italy and Portugal. On 6-8 July, these countries' prime ministers met to establish a common strategy in the new EU budget negotiations.

Conclusions. The Sánchez cabinet is fighting the economic crisis spending significantly on social measures and stimulating the economy. This policy requires an increase in taxes, but this solution also risks weakening investments (in the case of an increase in CIT) and consumption (VAT), which may limit GDP growth. Moreover, if the SURE mechanism isn't introduced by 30 September, the government may not extend ERTE, which will lead to a sharp rise in unemployment. In addition, fighting the pandemic and the economic crisis simultaneously require a temporary centralisation of management with the state, which cost the government regional parties' support and force it to negotiate compromises with the opposition.

The deepening crisis will force the Sánchez government to advocate for the rapid delivery of EU funds to save the economy. Given this pressure, Spain and its allies achieved what they needed from the new EU budget, which assumes €140 million in EU aid for Spain, including €72.7 million in grants. However, if these funds prove insufficient to restore the Spanish economy, the crisis in the eurozone will be exacerbated as Spain's market accounts for €150 billion in goods from eurozone countries—mainly from Germany, France, and Italy.

Editors: Sławomir Dębski, Patrycja Sasnal, Rafał Tarnogórski, Sebastian Płóciennik, Justyna Szczudlik, Daniel Szeligowski,
Jolanta Szymańska, Marcin Terlikowski, Karol Wasilewski, Szymon Zaręba, Tomasz Żornaczuk